

# Euro wrap-up

## Overview

- Bunds made losses despite news that German GDP contracted in the final quarter of 2021.
- Gilts also made losses as UK GDP growth in November beat expectations.
- The coming week brings the account of the ECB's December monetary policy account as well as new data for the UK's labour market, inflation and retail sales.

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### Daily bond market movements

Bond	Yield	Change
BKO 0 12/23	-0.601	+0.015
OBL 0 10/26	-0.377	+0.030
DBR 0 02/32	-0.056	+0.038
UKT 0 <sup>1</sup> / <sub>8</sub> 01/24	0.774	+0.027
UKT 0 <sup>3</sup> / <sub>8</sub> 10/26	0.955	+0.026
UKT 0 <sup>1</sup> / <sub>2</sub> 07/31	1.140	+0.037

\*Change from close as at 4:30pm GMT.  
Source: Bloomberg

## Euro area

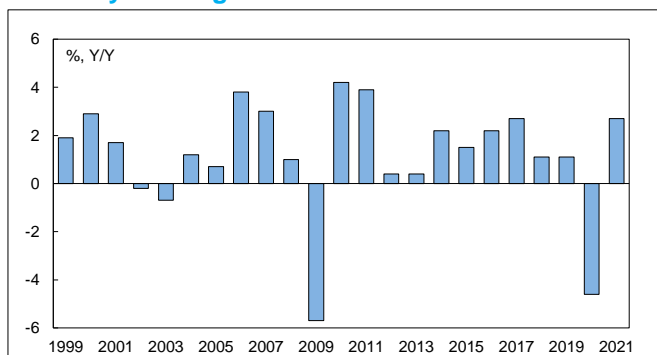
### German GDP contracted in Q4 to cap tepid year

In line with expectations, today's full-year German GDP data for 2021 reported calendar-adjusted growth of 2.7%Y/Y. That was a marked improvement from the (downwardly revised) contraction of 4.6%Y/Y in 2020 but disappointingly a full percentage point softer than had been anticipated by the Bundesbank in June before supply-chain bottlenecks took an increasing toll. And it will probably prove to be roughly 2ppts softer than growth in France, Italy and Spain last year. Indeed, although the preliminary estimate for last quarter will not be released until a fortnight's time, the Federal Statistical Office Destatis stated that GDP contracted 0.5-1.0%Q/Q in Q4. Within the detail on the expenditure side, over the year as a whole, household consumption was disappointingly unchanged from 2020 when it fell a record 5.9%Y/Y. And having dropped 2.2%Y/Y in 2020, gross fixed investment rebounded only 1.3%Y/Y last year with spending on machinery and investment (up 3.2%Y/Y) regaining little of the lost ground in 2020 (when it fell 11.2%Y/Y) and construction investment growth slowing 2.0ppts to just 0.5%Y/Y. Exports and imports of goods and services broadly reversed the steep declines of 2020, rising 9.4%Y/Y and 8.6%Y/Y respectively so that net trade added 0.9ppt to GDP growth. On the production side, of the major sectors, business services saw the strongest growth (5.4%Y/Y), with growth in manufacturing firm (4.4%Y/Y) and growth in several other services (e.g. ICT, trade, transport, hospitality and public services) also 3.0%Y/Y or more. We currently forecast a moderate pickup in German GDP growth to 3.4%Y/Y this year, just 0.2ppt below the forecast of the government but 0.2ppt above that of the Bundesbank and probably still more than 2.0ppts above the potential rate.

### German budget deficit somewhat smaller than expected

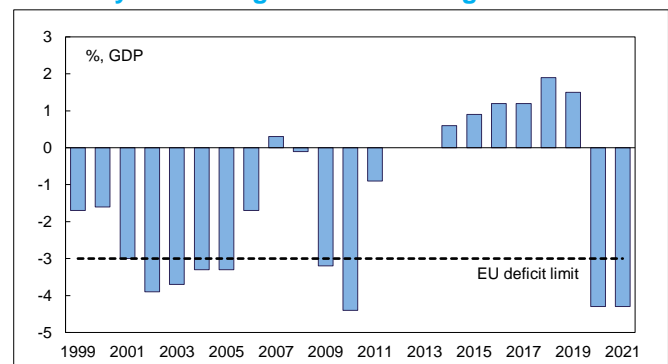
German GDP growth in 2021 would have been even softer had it not been for another sizeable increase in public spending. Indeed, boosted by the response to the pandemic, not least vaccination and Covid-19 testing programmes, government consumption rose a firm 3.4%Y/Y – the third consecutive year of growth of 3.0%Y/Y or above. However, as in 2020, and despite the softer-than-expected GDP growth, Germany's general government budget deficit in 2021 was significantly smaller than had been predicted. Indeed, today's data revealed that the deficit came in at 4.3% of GDP, the same (downwardly revised) level as in 2020, and roughly 3ppts lower than predicted in the Finance Ministry's Draft Budgetary Plan just three months ago. So, while the Plan also predicted that the budget deficit would decline significantly to around 3¼% of GDP in 2022 thanks to the ending of pandemic-related support programmes and healthcare spending, a figure well below the Stability and Growth Pact's benchmark of 3% of GDP seems highly likely this year.

### Germany: GDP growth\*



\*Calendar adjusted. Source: Destatis and Daiwa Capital Markets Europe Ltd.

### Germany: General government budget balance



Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Euro area records goods trade deficit for first time since 2011

Despite an improvement in export performance amid a pickup in [manufacturing output](#), today's euro area goods trade numbers showed a larger than expected drop in the trade balance in November, by €3.1bn to a deficit of €1.3bn, the first since 2011. This was in spite of an increase of 3.0%M/M in the value of exports, the largest monthly increase since September 2020, to leave then 14.5% higher than a year earlier. Within the country breakdown, there was strong growth in shipments to the UK (5.0%M/M), Switzerland (4.3%M/M), Norway (9.5%M/M) and Turkey (9.0%M/M), offsetting a notable weakening in exports to Asia as well as a modest drop to the US. Overall in October and November, export values were almost 4% higher than the Q3 average. Despite subdued growth in imports from the UK, the total value of imports jumped 4.5%M/M for the second successive month, to leaving them trending so far in Q4 roughly 8½% higher than the Q3 average. Of course, to some extent this reflects higher import prices, particularly of energy, which rose a further 1.6%M/M in November to be 23.4% higher than a year ago. But the volumes numbers for October suggested that growth in imports (4.7%M/M) significantly outpaced exports (2.4%M/M) at the start of the fourth quarter, raising some uncertainties about the extent to which net trade will provide a boost to GDP growth in Q4.

## The week ahead in the euro area

The euro area highlight of the coming week will be the publication of the account of the final [ECB monetary policy meeting](#) of 2021 on 16 December, when the Governing Council decided to slow its net asset purchases steadily over the course of this year. In particular, the account will likely confirm that the decision to end the net PEPP purchases at the end of March was widely endorsed but that a range of views existed with respect to the plans for regular APP purchases thereafter. The account will also probably highlight differing views regarding the chances that the preconditions for a rate hike might be met later this year or – more likely – in 2023.

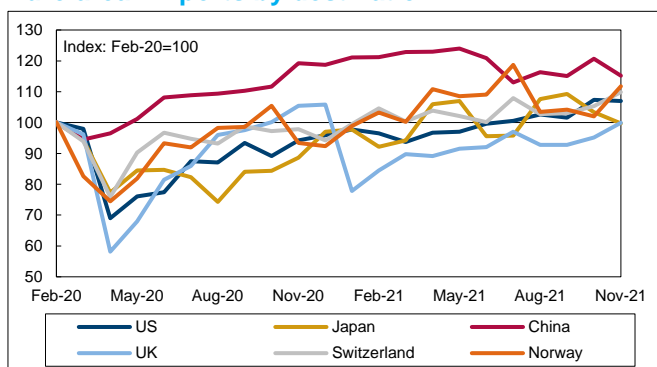
Data-wise, the coming week's euro area calendar is relatively light kicking off on Monday with the release of the final December consumer price inflation numbers for Italy, followed by the equivalent German and euro area inflation data on Wednesday and Thursday respectively. These data are expected to align with the flash figures, which suggested that euro area headline inflation edged up 0.1ppt in December to a new series high of 5.0%Y/Y, confounding expectations of a marginal drop. Meanwhile, Germany's ZEW investor sentiment survey (Tuesday) is expected to align with the [Sentix investor confidence](#) survey results and suggest a slightly more upbeat assessment at the start of the New Year, reflecting the view that the economic impact of the Omicron variant will be less severe than previously feared. Friday's Commission survey of preliminary consumer confidence for January will tell us if households share this optimism. Other data due to be published include EU-27 new car registrations for December on Tuesday, as well as euro area construction output for November on Wednesday, which is likely to have dropped led by declines in Germany and France.

## UK

### UK GDP beat expectations, with output back above the pre-pandemic level for the first time

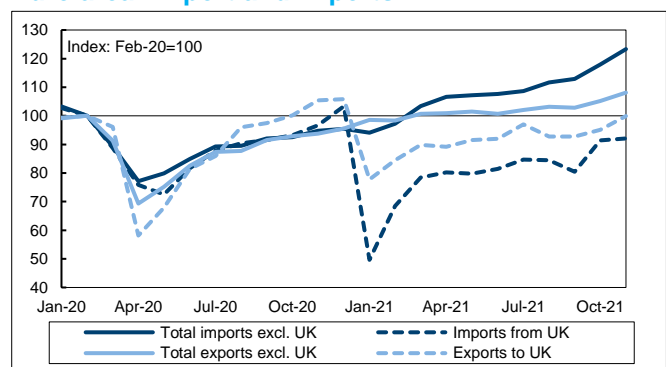
UK GDP beat expectations in November, rising 0.9%M/M following (upwardly revised) growth of 0.2%M/M in October. As a result, the average level of GDP in the first two months of Q4 was some 1.1% above the Q3 average, all but guaranteeing that quarterly GDP growth remained above-potential in the final quarter of the year despite the latest wave of Covid-19 and more stringent restrictions. Moreover, the growth in November took the level of GDP above its pre-pandemic level in February 2020 for the first time and by a non-negligible 0.7%. Due to the spread of Omicron, GDP will have fallen back in December and remained relatively subdued in January. And looking further ahead, concerns remain about the impact of declining real disposable incomes on the outlook for consumption. But while next week's labour market and inflation data will also have an important bearing on next month's monetary policy decision, the BoE is likely to take some comfort from today's figures, which suggest that underlying economic growth momentum is sufficiently firm to allow for another rate hike this quarter.

**Euro area: Exports by destination\***



\*Values. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

**Euro area: Export and imports\***



\*Values. Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

## Solid growth in services driven by retail and healthcare

Within the detail of the report, growth in November was broad-based, with all major sectors providing support. Given its large size, the services sector made the largest contribution to growth in November (more than 0.5ppt), rising 0.7%M/M to be 1.3% above the pre-pandemic level, with just over half of services subsectors back above the February 2020 level too. A key source of growth in the sector in November was retail, output of which rose 1.4% as consumers appeared to bring forward Christmas shopping amid fears of supply disruption closer to the festive season. That also gave a boost to transport and storage services, while professional, scientific and technical activities were very strong. Covid-19 vaccinations and test-and-trace activity added 0.2ppt to GDP growth. But despite a better showing in November, consumer-facing services remained some 5.0% below the pre-pandemic level, while other services were up 2.9% on the same basis, illustrating the continued impact of Covid-19 on such activities.

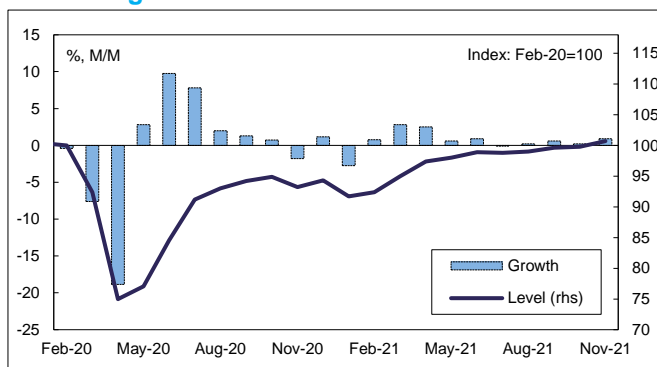
## Easing supply constraints give boost to manufacturing and construction too

While production rose 1.0%M/M in November after two months of negative growth, it was still some 2.6% below the pre-pandemic level (with manufacturing down 2.2% on that basis). Manufacturing output rose 1.1%M/M in November led by the autos subsector (up 7.8%M/M) as supply restraints appeared to ease somewhat, while other machinery and equipment rose 7.4%M/M. In contrast, mining and quarrying declined in November by 1.3%M/M due to declines in extraction of crude petroleum and natural gas. But with supply chain bottlenecks easing, construction output jumped 3.5%M/M, the most since March, to be 1.3% above the pre-pandemic level.

## Net trade on track to boost GDP growth in Q4, despite softer exports in November

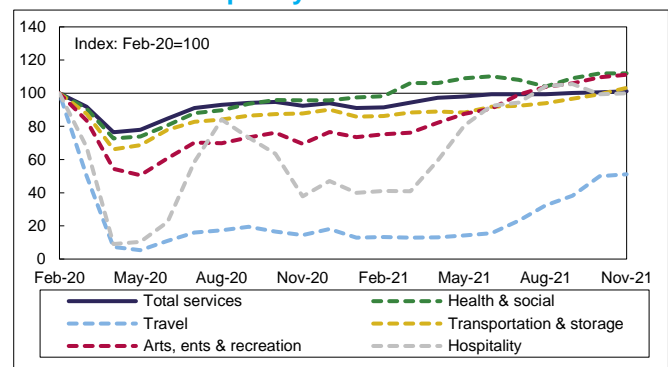
At face value, today's report also appeared to point to a markedly improved trade position in November, with the headline trade balance rising to a surplus of £624mn, the highest since August 2020. However, this largely reflected trade in precious metals and other erratic items – indeed, when excluding such items, the deficit widened a little more than £3bn to £5.1bn. When also adjusting for prices, the volume of goods exports fell 1.0%M/M, with services exports up just 0.2%M/M. Nevertheless, coming on the back of strong growth in October, this left export volumes trending almost 4% higher compared with the Q3 average (+7½% when including erratics). And with import volumes up around 3% on an equivalent basis (down more than ½% including erratics), today's report suggests that net trade was on track to provide a boost to GDP growth in Q4.

### UK: GDP growth and level



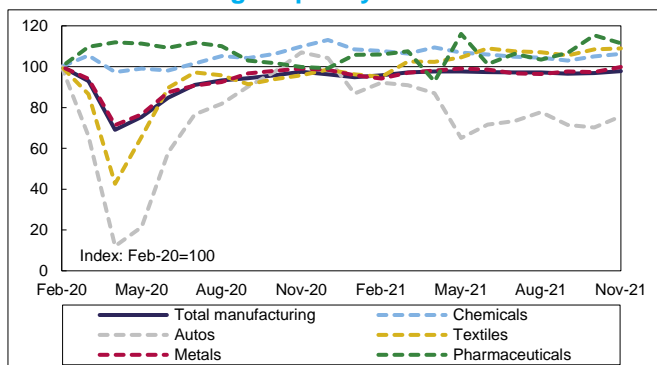
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### UK: Services output by selected subsector



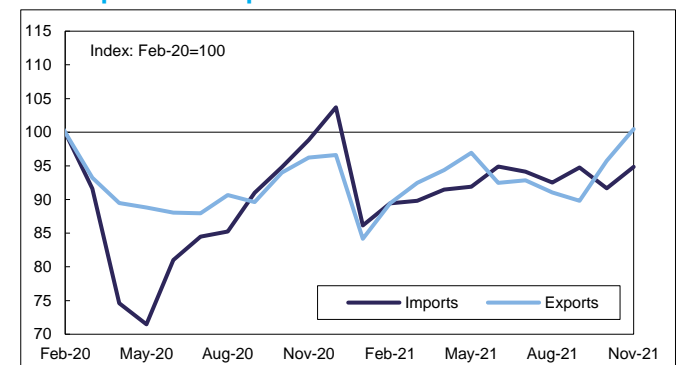
Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### UK: Manufacturing output by selected subsector



Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

### UK: Export and import volumes














Source: Refinitiv and Daiwa Capital Markets Europe Ltd.

## The week ahead in the UK

The coming week will also bring some key UK economic data that might provide further clarity on the near-term outlook for monetary policy ahead of the BoE's next MPC meeting in early February, including the latest labour market (Tuesday), inflation (Wednesday) and retail sales (Friday) reports. Of particular interest in the labour market data will be the monthly payrolls numbers for December, which seem bound to have slowed from the near-250k increase seen in November due to the Omicron variant and tighter pandemic-related restrictions. But with vacancies still near record highs, wage growth is expected to have eased only slightly further in the three months to November, and remain above the pre-pandemic average. Nevertheless, given rising inflation, real wage growth is likely to have fallen further into negative territory. In terms of inflation, we expect the headline CPI rate to have risen further in December, by 0.3ppt to 5.4%Y/Y, in part reflecting higher food price inflation. Core inflation is forecast to move sideways at 4.0%Y/Y. Turning to retail sales, December's release is expected to show that, following strong growth in November and weaker consumer confidence amid the surge in coronavirus cases, sales fell back at the end of last year, albeit not fully reversing the near-1½%M/M increase seen in November. And the latest GfK consumer confidence survey (Friday) seems unlikely to point to any substantial improvement in sentiment at the start of the year either. Other releases include the Rightmove, ONS and RICS housing market indicators on Monday, Wednesday and Thursday respectively.

The next edition of the Euro wrap-up will be published on 18 January 2022

## Daiwa economic forecasts

	2021		2022				2021	2022	2023
	Q3	Q4	Q1	Q2	Q3	Q4			
<b>GDP forecasts % , Q/Q</b>									
Euro area 	2.2	0.3	0.2	1.5	1.0	0.7	5.1	3.9	2.7
UK 	1.1	0.9	0.3	1.0	0.8	0.6	7.2	4.1	1.9
<b>Inflation forecasts % , Y/Y</b>									
Euro area									
Headline CPI 	2.8	4.6	4.1	4.2	3.5	2.0	2.6	3.4	1.8
Core CPI 	1.4	2.4	2.1	2.9	2.5	1.9	1.5	2.4	1.7
UK									
Headline CPI 	2.8	4.9	5.4	5.3	4.6	2.8	2.6	4.5	1.9
Core CPI 	2.6	3.8	4.2	3.7	3.1	2.1	2.4	3.3	2.0
<b>Monetary policy</b>									
ECB									
Refi Rate % 	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Deposit Rate % 	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
PEPP envelope* (€bn) 	1850	1850	1850	1850	1850	1850	1850	1850	1850
BoE									
Bank Rate % 	0.10	0.25	0.50	0.50	0.75	0.75	0.25	0.75	1.25
Gilt purchases* (£bn) 	875	875	850	850	840	840	875	840	810

\*Target end of period. Source: Bloomberg, ECB, BoE and Daiwa Capital Markets Europe Ltd.

















## The coming week's data calendar

### The coming week's key data releases

Country	GMT	Release	Period	Market consensus/ <i>Daiwa</i> <i>forecast/actual</i>	Previous
<b>Monday 17 January 2022</b>					
Italy	10.00	Final CPI (EU harmonised CPI) Y/Y%	Dec	3.9 (4.2)	3.7 (3.9)
UK	00.01	Rightmove house price index M/M% (Y/Y%)	Jan	-	-0.7 (6.3)
<b>Tuesday 18 January 2022</b>					
Euro area	07.00	EU27 new car registrations Y/Y%	Dec	-	-20.5
Germany	10.00	ZEW survey current situations (expectations) balance	Jan	-10.5 (33.0)	-7.4 (29.9)
Italy	10.00	Trade balance €bn	Nov	-	3.9
UK	07.00	Claimant count rate % (change 000s)	Dec	-	4.9 (-49.8)
	07.00	Payrolled employees monthly change 000s	Dec	-	257
	07.00	ILO unemployment rate 3M% (employment change 3M 000s)	Nov	4.2 (129)	4.2 (149)
	07.00	Average weekly earnings (excluding bonuses) 3M/Y%	Nov	4.2 (3.7)	4.9 (4.3)
<b>Wednesday 19 January 2022</b>					
Euro area	10.00	Construction output M/M% (Y/Y%)	Nov	-	1.6 (4.4)
Germany	07.00	Final CPI (EU harmonised CPI) Y/Y%	Dec	5.3 (5.7)	5.2 (6.0)
UK	07.00	CPI (core CPI) Y/Y%	Dec	<u>5.4 (4.0)</u>	5.1 (4.0)
	07.00	PPI input prices (output prices) Y/Y%	Dec	13.6 (9.3)	14.3 (9.1)
	09.30	House price index Y/Y%	Nov	-	10.2
<b>Thursday 20 January 2022</b>					
Euro area	10.00	Final CPI (core CPI) Y/Y%	Dec	5.0 (2.6)	4.9 (2.6)
Germany	07.00	PPI M/M% (Y/Y%)	Dec	0.9 (19.2)	0.8 (19.2)
France	07.45	INSEE business (manufacturing) confidence	Jan	109 (112)	110 (111)
Spain	09.00	Trade balance €bn	Nov	-	-3.4
UK	00.01	RICS house price balance %	Dec	70	71
<b>Friday 21 January 2022</b>					
Euro area	15.00	Commission's preliminary consumer confidence	Jan	-9.0	-8.3
UK	00.01	GfK consumer confidence	Jan	-16	-15
	07.00	Retail sales M/M% (Y/Y%)	Dec	-0.5 (3.5)	1.4 (4.7)
	07.00	Retail sales, excluding auto fuel M/M% (Y/Y%)	Dec	-0.5 (1.3)	1.1 (2.7)

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.











## The coming week's key events &amp; auctions

Country	GMT	Event / Auction
<b>Monday 17 January 2022</b>		
Euro area 	-	ECB President Lagarde and Governing Council member Panetta take part in Eurogroup meeting
<b>Tuesday 18 January 2022</b>		
Euro area 	-	ECB's Vice President de Guindos takes part in ECOFIN meeting
Germany 	10.30	Auction: €4bn of 0% 2027 bonds
UK 	10.00	Auction: £2.5bn of 0.5% 2029 bonds
<b>Wednesday 19 January 2022</b>		
Germany 	10.30	Auction: €1.5bn of 0% 2036 bonds
UK 	14.15	BoE officials to appear before the Treasury Select Committee to discuss the Financial Stability Report
<b>Thursday 20 January 2022</b>		
Euro area 	12.30	ECB publishes account of 16 December Governing Council meeting
France 	09.50	Auction: 0% 2027 bonds
	09.50	Auction: 0.75% 2028 bonds
	09.50	Auction: 0% 2025 bonds
	09.50	Auction: 0.1% 2026 inflation-linked bonds
	09.50	Auction: 0.1% 2031 inflation-linked bonds
	09.50	Auction: 0.1% 2032 inflation-linked bonds
Spain 	09.30	Auction: to sell bonds with various maturities
<b>Friday 21 January 2022</b>		
Euro area 	12.30	ECB President Lagarde takes part in a forum on 'The Global Economic Outlook'
UK 	13.00	BoE MPC member Mann to speak at an event on the economy and monetary policy

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

## Today's results

## Economic data

Country	Release	Period	Actual	Market consensus/ Daiwa forecast	Previous	Revised
Euro area 	Trade balance €bn	Nov	-1.3	1.5	2.4	1.8
Germany 	GDP Y/Y%	2021	2.7	2.7	-5.0	-4.6
France 	Final CPI (EU-harmonised CPI) Y/Y%	Dec	2.8 (3.4)	2.8 (3.4)	2.8 (3.4)	-
Spain 	Final CPI (EU-harmonised CPI) Y/Y%	Dec	6.5 (6.6)	6.7 (6.7)	5.5 (5.5)	-
UK 	GDP M/M% (3M/3M%)	Nov	0.9 (1.1)	0.4 (0.8)	0.1 (0.9)	0.2 (-)
	Industrial production M/M% (Y/Y%)	Nov	1.0 (0.1)	0.2 (0.5)	-0.6 (0.4)	-0.5 (0.2)
	Manufacturing production M/M% (Y/Y%)	Nov	1.1 (0.4)	0.2 (-0.3)	0.0 (1.3)	0.1 (1.1)
	Index of services M/M% (3M/3M)	Nov	0.7 (1.3)	0.5 (1.1)	0.4 (1.1)	-(1.2)
	Construction output M/M% (Y/Y%)	Nov	3.5 (6.8)	0.6 (3.1)	-1.8 (3.3)	-1.7 (4.3)
	Goods trade balance £bn	Nov	-11.3	-14.2	-13.9	-11.8

## Auctions

Country	Auction
- Nothing to report -	

Source: Bloomberg and Daiwa Capital Markets Europe Ltd.

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